Iowa Code section 422.42(13) defines a person engaged in the business of performing taxable services as a retailer. Since retailers may purchase building materials, supplies and equipment for resale, persons making taxable repairs (repairpersons and servicepersons) are not considered to be contractors and are not subject to the provisions of Iowa Code section 422.42(15). In addition, such persons are not considered to be owners, subcontractors or builders. So repairpersons and servicepersons will normally purchase building materials and supplies free of tax for subsequent resale to their customers; contractor-retailers will also do this. However, contractors, subcontractors or builders who may make repairs are subject to Iowa Code section 422.42(15) and must pay tax at the time building materials, supplies and equipment are purchased from their vendors even though they hold a valid sales tax permit. See rules 19.2(422,423) and 19.3(422,423). In determining who is a contractor and who is a retailer of repair services, the department looks to the "total business" of the entity in question and not to any one portion of it. Thus, the fact that a business whose overall activity is contracting has a division engaged in taxable repair services does not transform that business into a retailer providing services rather than a contractor. When contractors do repair work, they should separately itemize labor and materials charges and collect sales tax on labor charges only. A contractor's markup on a materials charge is not part of any taxable labor charge unless that markup is a disguised labor charge done with the intent to evade collecting Iowa sales tax.

When other persons making repairs sell tangible personal property at retail in connection with any taxable service enumerated in Iowa Code section 422.43, then those persons shall collect and remit tax on all gross receipts. The person making repairs shall purchase tangible personal property for resale when the property is used in the repair job and is resold to a customer. See rule 701—18.31(422,423) for an explanation of when persons performing services sell the property they use in performing those services to their customers. Nonexclusive examples of repair situations follow:

1. Repair of broken or defective glass.
2. Replacement of broken, defective or rotten windows.
3. Replacing individual or damaged roof shingles.
4. Replacing or repairing a portion of worn-out or broken kitchen cabinets.
5. Replacement of garage doors or garage door openers.
6. Replacing or repairing a portion of a broken or worn tub, shower, or faucets.
7. Replacing or repairing a portion of a broken water heater, furnace or central air conditioning compressor.
8. Restoration of original wiring in a house or building.

19.13(2) The following are examples of new construction, reconstruction, alteration, expansion and remodeling activities:

a. The building of a garage or adding a garage to an existing building would be considered new construction.

b. Adding a redwood deck to an existing structure would be considered new construction.

c. Replacing a complete roof on an existing structure would be considered new construction or alteration.

d. Adding a new room to an existing building would be considered new construction.

e. Adding a new room by building interior walls would be considered alteration.

f. Replacing kitchen cabinets with some modification would be considered an improvement.

g. Paneling existing walls would be considered an improvement.

h. Laying a new floor over an existing floor would be considered an improvement.

i. Rebuilding a structure damaged by flood, fire or other uncontrollable disaster or casualty would be considered reconstruction.

j. Building a new wing to an existing building would be considered an expansion.

k. Rearranging the interior structure of a building would be considered remodeling.

l. Installing manufactured housing or a modular or mobile home on a foundation. However, see rule 701—33.10(423) for a description of the special treatment of taxable installation charges when the taxable sale of manufactured housing as real estate occurs.

m. Replacing an entire water heater, water softener, furnace or central air conditioning unit.

n. Sign installation and well-drilling services are generally performed in connection with new construction.

In all the examples, the contractor is responsible for paying tax to any supplier on materials. However, there would be no tax on any enumerated services.

19.13(3) The term "on or connected with" is broad and should be used to convey generally accepted meaning. Therefore, in a specific situation, the facts relating thereto are controlling in determining whether the exemption is applicable. "On or connected with" does not connote that those things connected have to be primary or subsidiary to the construction, reconstruction, alteration, expansion or remodeling of the real property. An incidental relationship can qualify the activity for exemption if the relationship forms an intimate connection with the construction activity. For example, the service of excavating and grading relating to the clearing of land to begin construction of a building would qualify for the exemption; however, excavating and grading land without motive toward construction would not qualify for exemption even though at some later date plans to construct a building were created and a structure was actually erected.

The presence of a time relationship can also be a factor in determining the applicability of exemption. For example, tax would not apply to separate labor charges relating to the installation of production machinery and equipment in a building while remodeling of the real property was in progress. (Tax could apply to the sales price of the production machinery and equipment; see rule 701—18.45(422,423).) However, if a year after all construction activity has ended, the owner decides to install a piece of production machinery in the building, any taxable enumerated services relating thereto would be subject to tax. Further, if following construction, the land is graded for the purpose of seeding a new lawn, the exemption would be applicable. However, if the lawn does not grow and the land is regraded the following year, the exemption would not be applicable. See also 701—subrule 18.45(7) for the exemption, effective July 1, 1985, regarding the installation of new industrial machinery and equipment.

Therefore, the motive behind the activity and the course of events that could reasonably be expected to occur would be a further consideration in determining if the exemption is applicable.

A physical relationship is also a factor that should be evaluated. If a building is constructed to house machinery, any enumerated services relating to the installation of that machinery would be exempt from tax. For example, piping joining two pieces of equipment housed in separate buildings would qualify for exemption if the equipment in either building was installed while such new construction, reconstruction, alteration, expansion or remodeling to the structure was also taking place to house the equipment.

On the other hand, an incidental relationship, a time relationship and close physical proximity may not be enough to support the conclusion that a taxable service is performed in connection with new construction or reconstruction, for example. For instance, a homeowner hires a general contractor to add a new room to an existing home (which is new construction; see 19.13(2)*"d"* above). The existing home is in need of a number of the repairs described in 19.13(1); for example, it is in need of rewiring and replacement of a broken window. The general contractor rewires the home and repairs the window in addition to building the new room. The taxable services which the general contractor performs while rewiring the home and repairing the window are not performed in connection with the construction of the new room simply because those services happen to be performed at the same time and on the same home as the new construction. If the addition of the new room were the cause of the need for the taxable service (e.g., the window was broken during construction of the new room) and not just a convenient occasion for performance of the service, that performance would be exempt from tax.

The department would like to emphasize that facts and motives are important in the determination of the taxability of services relating to construction activities. However, it should also be noted that taxes on enumerated services are applicable to repair work that is not a construction activity. Please refer to subrule 19.13(1) relating to persons who make repairs for more information.

19.13(4) Excavating includes the digging, hollowing out, scooping out, or making a hole in the earth. It also includes removal of materials or substance found beneath the surface. Grading includes a change in the earth's structure by scraping and filling to a common level or a fixed line known as a grade. The enumerated services excavating and grading are not subject to tax if performed on or connected with new construction. Removal of overburden which is directly related to road building, building of dikes, building of farm ponds, and creating drainage ditches would not be taxable as such activities would be considered on or connected with the creation of a structure. See *Maasdam v. Kirkpatrick*, 214 Iowa 1388 (1932). However the mere removal of overburden, without more, would be taxable as the enumerated service of excavating or grading under Iowa Code section 422.43.

19.13(5) Services associated with new construction or reconstruction, for example, which are not taxable include, but are not limited to, brick laying, concrete finishing, tiling, siding installation, laying of linoleum and other flooring and carpet installation. No tax can be collected on the performance of these services even when they are furnished in connection with the performance of repairs.

This rule is intended to implement Acts of the Sixty-third General Assembly, First Session, 1969, chapter 248, section 9 (this enactment is not part of the Iowa Code).

701—19.14(422,423) Transportation cost. Transportation charges and delivery charges are not subject to the Iowa sales and use tax when they are separately contracted or, if no written contract exists, are separately itemized on the billing from the seller to the purchaser. See rule 701—15.13(422,423).

701—19.15(422,423) Start-up charges. Start-up charges are not subject to the Iowa sales and use tax when they are separately contracted or, if no written contract exists, are separately itemized on the billing from the seller to the purchaser.

701—19.16(422,423) Liability of subcontractors. A subcontractor who is providing materials and labor on the actual construction of the building or structure has the same status and tax responsibilities as a general contractor under the Iowa statutes. However, where an individual or firm is hired to provide machinery and equipment to a general contractor or another subcontractor, the individual or firm is considered a material supplier rather than a subcontractor. This is true, even though the machinery and equipment are supplied with installation. Items of machinery and equipment sold by material suppliers to contractors shall be sold for resale and the contractor must provide the material supplier with a valid resale certificate.

701—19.17(422,423) Liability of sponsors. The sponsor cannot be held responsible for a tax liability incurred on building materials, supplies and equipment by a general contractor or subcontractor in the completion of a construction contract. Likewise, a general contractor cannot be held responsible for the tax liability incurred on building materials, supplies and equipment by a subcontractor in the completion of a construction contract. The tax responsibility regarding machinery and equipment contracts depends on where the sale was consummated. If the sale was consummated in Iowa, the seller is responsible for the collection and remittance of tax unless a valid exemption certificate is given by the purchaser. If the sale was consummated outside Iowa and the seller does not remit use tax to the department, then a use tax would be due from the Iowa user.

701—19.18(422,423) Withholding. A sponsor of a contract with a nonregistered out-of-state (nonresident) contractor may be asked to withhold the final payment of the contract as a guarantee that sales and use taxes will be paid. The withholding requirement may also apply to registered out-of-state contractors at the discretion of the department. The department will issue a notice to the sponsor to support the withholding of funds. In order to seek a release of the notice, the out-of-state contractor is required to file a report with the department consisting of the following departmental forms:

1. Form 35-012 which is a listing of subcontractors to whom the out-of-state contractor has awarded a construction contract. This statement should be submitted on each project as it becomes available.
2. Form 35-013 which is a list of material suppliers both in state and out of state from whom tangible personal property has been purchased for use in completing each project or contract.
3. Form 35-001 which is a summary of the provisions of the actual contract.

All letters of release furnished by the department are subject to audit and therefore, are not unconditional release from any Iowa sales or use tax liability. All letters of release will be issued within 60 days upon receipt of the proper information unless an error or discrepancy is noted.

701—19.19(422,423) Resale certificates. Whenever machinery and equipment which will remain tangible personal property after installation is purchased for a machinery and equipment contract, by a contractor from a supplier or a material supplier, it should be purchased for resale. See rule 19.8(422,423). Resale purchases are most commonly related to machinery and equipment sales contracts with installation and mixed construction contracts. Contractor-retailers and persons making repairs may also purchase materials for resale as long as they collect tax on their retail sales and pay the tax themselves on items withdrawn from inventory for use in the performance of a construction contract. See rule 19.4 (422, 423) and subrule 19.13(1). Resale certificates can be obtained by contacting the Iowa department of revenue and finance. See rule 701—15.3(422,423) for detailed information on resale certificates.

701—19.20(423) Reporting for use tax. An Iowa contractor can report use tax either on a consumers use tax return or as consumed goods on a sales tax return. Tax is due in the quarter the materials are delivered into Iowa. Nonresident contractors should report use tax on a consumers use tax return. Consumer use tax returns for nonresident contractors must be obtained directly from the department of revenue and finance unless the contractor is registered with the department.

This chapter is intended to implement Iowa Code sections 422.42(3), 422.42(12), 422.42(13), 422.43, 422.45(5), 422.45(7), 422.45(8), 422.47, 422.48, and 423.2.

[Filed 12/12/74]
[Filed 9/2/77, Notice 6/15/77—published 9/21/77, effective 10/26/77]
[Filed 4/28/78, Notice 3/22/78—published 5/17/78, effective 7/1/78]
[Filed 3/28/80, Notice 2/20/80—published 4/16/80, effective 5/21/80]
[Filed 3/13/81, Notice 2/4/81—published 4/1/81, effective 5/6/81]
[Filed 3/25/82, Notice 2/17/82—published 4/14/82, effective 5/19/82]
[Filed emergency 2/9/83—published 3/2/83, effective 3/1/83]
[Filed 2/10/83, Notice 1/5/83—published 3/2/83, effective 4/6/83]
[Filed 4/22/83, Notices 3/2/83, 3/16/83—published 5/11/83, effective 6/15/83]
[Filed 9/9/83, Notice 8/3/83—published 9/28/83, effective 11/2/83]

[Filed emergency 11/14/86—published 12/17/86, effective 11/14/86]
[Filed 3/3/88, Notice 1/27/88—published 3/23/88, effective 4/27/88]
[Filed 9/30/88, Notice 8/24/88—published 10/19/88, effective 11/23/88]
[Filed 11/22/89, Notice 10/18/89—published 12/13/89, effective 1/17/90]
[Filed 8/30/90, Notice 7/25/90—published 9/19/90, effective 10/24/90]
[Filed emergency 7/1/92—published 7/22/92, effective 7/1/92]
[Filed 8/28/92, Notice 7/22/92—published 9/16/92, effective 10/21/92]
[Filed 11/6/92, Notice 9/30/92—published 11/25/92, effective 12/30/92]
[Filed 11/27/96, Notice 10/23/96—published 12/18/96, effective 1/22/97]
[Filed 10/30/98, Notice 9/23/98—published 11/18/98, effective 12/23/98]
[Filed 12/10/99, Notice 11/3/99—published 12/29/99, effective 2/2/00]
[Filed 10/26/01, Notice 9/19/01—published 11/14/01, effective 12/19/01]
[Filed 1/17/03, Notice 12/11/02—published 2/5/03, effective 3/12/03]